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315201—41

In the Supreme Court of the United States

OCTOBER TERM, 1940

No. 964

WILLIAM LARIMER MELLON AND THOMAS MELLON, EXECUTORS OF THE WILL OF JAMES R. MELLON, DECEASED, PETITIONERS

v.

WILLIAM DRISCOLL, COLLECTOR OF INTERNAL REVENUE FOR THE TWENTY-THIRD DISTRICT OF PENNSYLVANIA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court (R. 2–14) is unreported. The opinion of the Circuit Court of Appeals (R. 22–28) is reported in 117 F. (2d) 477.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered February 3, 1941. (R. 28.) The petition for a writ of certiorari was filed on April 18,

1941. The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Prior to the enactment of Section 302 (d) of the Revenue Act of 1926, the decedent established two spendthrift trusts. In each a child was given the income for life and a testamentary power to dispose of the principal; if the power was not exercised, the principal would go to the life beneficiary's heirs under the intestacy laws of Pennsylvania. The decedent, however, reserved the power to revoke each trust, after six months' notice, in which event the principal would be distributed to the life beneficiary and the trust would end. The question is whether by virtue of this reservation the decedent's interests in the trust were properly included in his gross estate under Section 302 (d) of the Revenue Act of 1926, as amended.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix, *infra,* pp. 9–14.

STATEMENT

The decedent, James R. Mellon, died October 20, 1934. (R. 3.) In 1917, he had created two trusts, one for the benefit of each of his children, Thomas R. Mellon and S. Lucille Mellon Grange. (R. 4–5.)

The trustee in each instance was directed to pay the income to the child for life, and upon the child's

death to distribute the principal and undistributed income to such persons as the life beneficiary designated by his last will and testament. In the absence of such direction, the trustee was directed to distribute the property to such persons as would take as the life beneficiary's heirs under the intestacy laws of Pennsylvania. (R. 16, 18.)

Each trust provided that (R. 16, 18):

> Neither the principal of the said trust estate nor the income thereof shall in any manner be liable to the control or answerable for the debts, contracts, engagements or torts of the said cestui que trust, or liable to any charge, assignment, conveyance or anticipation by him [her].

It was also provided in each trust that (R. 16–17, 19):

> The party of the first part hereby reserves the right after six months written notice of his intention so to do, served on the party of the second part, to revoke this trust, whereupon the principal of the trust fund shall be distributed to Thomas Mellon [S. Lucille Mellon Grange] and the trust shall end.

The Commissioner of Internal Revenue included in the decedent's gross estate the value of the trust funds less the value of the life estates, and determined a deficiency accordingly. (R. 5–6.) The petitioners, executors under the decedent's will, brought suit to recover the tax paid pursuant thereto. The Circuit Court of Appeals affirmed

a judgment of the District Court in favor of the Collector. (R. 28.)

ARGUMENT

The case presents a routine tax question, which was correctly decided by the courts below. The petitioners' claims that the decision is in conflict with *Estate of Sanford* v. *Commissioner,* 308 U. S. 39, and current administrative practice are without foundation. No conflict among the circuits is asserted. Accordingly, there is no occasion for further review.

1. It is plain that the enjoyment of the trust properties was at the decedent's death, subject to "change" through the exercise of a power "to alter, amend, or revoke" within the meaning of Section 302 (d) of the Revenue Act of 1926, as amended by Section 401 of the Revenue Act of 1934. Under the trusts, the decedent's children had a non-alienable right to the income for life and a testamentary power of appointment over the principal. If, on the other hand, the decedent's powers of revocation were exercised, the children would acquire unrestricted ownership of the trust estate. Thereafter they would have an unqualified right to the use of both principal and income, including the right of alienation *inter vivos* as well as testamentary; at the same time, they would lose the protection accorded them by the trusts against the claims of creditors. These differences between the interests of beneficiaries

of spendthrift trusts and absolute ownership are substantial.

2. The reserved powers were not outside the purview of the statute because their exercise would "terminate" the trusts. In common usage, there is no difference in substance between termination and revocation, and the trusts themselves describe the power as one to "revoke." If, however, the term "revoke" is construed to require a revesting of the estate in the settlor, the power here reserved would nevertheless be within the statute as one to "alter" the enjoyment of the property. See Regulations 80, Article 20, as amended by Treasury Decision 4729, Appendix, *infra*. Cf. *Commissioner* v. *Chase Nat. Bank*, 82 F. (2d) 157 (C. C. A. 2d), certiorari denied, 299 U. S. 552; *Holderness* v. *Commissioner*, 86 F. (2d) 137 (C. C. A. 4th); *Hoblitzelle* v. *United States*, 3 F. Supp. 331 (C. Cls.).

The argument that the statute did not include a power to terminate was made in *White* v. *Poor*, 296 U. S. 98, but the Court did not decide the point. In order that the question "should be set at rest", the statute was amended in 1936 specifically to include the word "terminate" after the words "alter, amend, or revoke". Revenue Act of 1936, Section 805.[1] The report of the House Committee on Ways

[1] The amendment, which was adopted in the Revenue Act of 1936 (H. R. 12395, 74th Cong., 2d Sess.), was originally introduced in the House as part of H. R. 12793, 74th Cong., 2d Sess., and was added to the 1936 Act in the Senate.

and Means expressed the belief that the amendment was merely declaratory of existing law,[2] and this has also been the interpretation given the amendment by the Treasury. Regulations 80, Article 20, as amended by T. D. 4729, Appendix, *infra*.

3. The petitioners' contention that the transfers were not subject to any power at the date of decedent's death because he had never given the six months' written notice required by the trusts is likewise without merit. The notice requirement was merely an incident to the exercise of the power which in nowise affected its substance. Any conceivable doubt on the question, however, is removed by the express provisions of the 1934 amendment to Section 302 (d). Revenue Act of 1934, Section 401. This amendment, designed to clarify existing law,[3] was in effect at the time of the decedent's death, and is plainly applicable.

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[2] H. Rep. No. 2818 on H. R. 12793, 74th Cong., 2d Sess., p. 10:

> Another change made in subsection (a) of section 206 has been to expressly include a power to terminate along with the powers to alter, amend, or revoke. In the case of *White* v. *Poor*, *supra*, the Supreme Court did not pass on the question of whether the power to terminate was included in the language relating to a power "to alter, amend or revoke." Since in substance a power to terminate is the equivalent of a power to revoke, this question should be set at rest. Express provision to that effect has been made and it is believed that it is declaratory of existing law.

[3] H. Rep. No. 704 on Revenue Act of 1934, 73d Cong., 2d Sess. (1939–1 Cum. Bull. Part 2), 581); Sen. Rep. No. 558 on Revenue Act of 1934, 73d Cong., 2d Sess. (1939–1 Cum. Bull. (Part. 2), 620).

The petitioner's argument, based on *Hassett* v. *Welch,* 303 U. S. 303, that the 1934 amendment does not apply to prior transfers, overlooks the fact that there the Court was concerned with the retroactive application of an amendment to Section 302 (c) taxing transfers in contemplation of death or intended to take effect in possession or enjoyment at death. The taxable event under Section 302 (d) is not the prior transfer but the termination by death of the reserved power. *Porter* v. *Commissioner,* 288 U. S. 436. Consequently, there is no retroactive application.

Moreover, application of the amendment is neither unfair nor arbitrary. The decedent was clearly put upon notice by the adoption of the amendment and he had ample opportunity to avoid the tax by releasing the power prior to his death. *Commissioner* v. *Chase Nat. Bank, supra; Witherbee* v. *Commissioner,* 70 F. (2d) 696 (C. C. A. 2d), certiorari denied, 293 U. S. 582.

4. The petitioners' contention that the decision of the court below conflicts with *Estate of Sanford* v. *Commissioner,* 308 U. S. 39, and current Treasury Regulations pertaining to the gift tax is based upon an incorrect premise, namely, that the estate tax and gift tax statutes must be construed as mutually exclusive except for transfers in contempla-

tion of death. The *Sanford* opinion implies other exceptions, and they unquestionably exist. For example, although transfers subject to a power of revocation exercisable jointly by the settlor and a person having an adverse interest are completed gifts (*Reinecke* v. *Northern Trust Co.*, 278 U. S. 339), they are nevertheless within the specific provisions of Section 302 (d) of the estate tax. *Helvering* v. *City Bank Co.*, 296 U. S. 85. While the statutes, to the extent appropriate, should be construed *in pari materia*, it does not follow, as the petitioners' contention assumes, that interpretations given the general language of the gift tax should limit the precise definitions employed in the estate tax. Accordingly, whether or not the decedent's transfers would have constituted a completed gift for purposes of a gift tax, there is no inconsistency which is not contemplated by the statutes and the relevant decisions.

CONCLUSION

The petition for certiorari should be denied.

Respectfully submitted.

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MAY, 1941.